

Auditor-General of South Africa

**Nelson Mandela Bay  
Metropolitan Municipality and its  
municipal entity**

**Audit report for the year ending  
30 June 2020**

# Report of the auditor-general to the Eastern Cape Provincial Legislature and the council on the Nelson Mandela Bay Metropolitan Municipality and its municipal entity

## Report on the audit of the consolidated and separate financial statements

### Qualified opinion

1. I have audited the consolidated and separate financial statements of the Nelson Mandela Bay Metropolitan Municipality and its municipal entity (group) set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2020, statement of financial performance, statement of changes in net assets and statement of cash flows for the year then ended, as well as the notes to the consolidated and separate financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the possible effects of the matters described in the basis for qualified opinion section of this auditor's report, the consolidated and separate financial statements present fairly, in all material respects, the financial position of the group as at 30 June 2020, and its financial performance and cash flows for the year then ended in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act 56 of 2003 (MFMA) and the Division of Revenue Act 16 of 2019 (Dora).

### Basis for qualified opinion

#### Property, plant and equipment

3. I was unable to obtain sufficient appropriate evidence that the municipality had appropriately accounted for and disclosed property, plant and equipment due to the status of the accounting records. Certain infrastructure assets and other assets could not be supported by complete and accurate underlying records and completed assets could not be substantiated by supporting audit evidence. I could not confirm infrastructure assets, other assets and completed assets by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to property, plant and equipment stated at R17,3 billion (2019: R17,4 billion) in the consolidated and separate financial statements.
4. The municipality also did not adequately assess whether there were any indications that the expectations on the useful lives of property, plant and equipment had changed in accordance with GRAP 17, *Property, plant and equipment*. Furthermore, completed assets were misclassified as work in progress, which was also contrary to this standard. I was unable to determine the impact on property, plant and equipment and depreciation stated at R958,3 million and R957,2 million (2019: R882,4 million and R881,7 million) in the consolidated and separate financial statements, respectively, as it was impracticable to do so. There was also an impact on the surplus for the period and on the accumulated surplus.

## Investment property

5. I was unable to obtain sufficient appropriate evidence for investment property as the underlying records maintained by the municipality were not complete to determine ownership of these properties. I was unable to confirm investment property through alternative means. Consequently, I was unable to determine whether any adjustments were necessary to investment property stated at R165,1 million (2019: R216,8 million) in the consolidated and separate financial statements.

## Unauthorised expenditure

6. During 2019, I was unable to obtain sufficient appropriate audit evidence for unauthorised expenditure and to confirm the unauthorised expenditure by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to unauthorised expenditure stated at R253 million in note 44.1 to the consolidated and separate financial statements. My audit opinion on the consolidated and separate financial statements for the prior year was modified accordingly. My opinion on the current year consolidated and separate financial statements was also modified because of the possible effect of this matter on the comparability of the unauthorised expenditure for the current period.

## Exchange revenue – service charges

7. During 2019, I was unable to obtain sufficient appropriate audit evidence that revenue from service charges had been properly accounted for as the municipality did not have adequate internal controls to maintain records for service charges. I was unable to confirm the revenue from service charges by alternative means. In addition, the municipality did not bill and record certain revenue owing to it for services rendered, as required by *GRAP 9, Revenue from exchange transactions* during 2019. Consequently, I was unable to determine whether any adjustment was necessary to the corresponding figure stated at R5,3 billion in the consolidated and separate financial statements. My audit opinion on the consolidated and separate financial statements for the prior year was modified accordingly. My opinion on the current year consolidated and separate financial statements was also modified because of the possible effect of this matter on the comparability of the exchange revenue – service charges for the current period.

## Context for the opinion

8. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the consolidated and separate financial statements section of this auditor's report.
9. I am independent of the group in accordance with the International Ethics Standards Board for Accountants' *International Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA code) as well as other ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.

10. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

### **Emphasis of matters**

11. I draw attention to the matters below. My opinion is not modified in respect of these matters.

### **Restatement of corresponding figures**

12. As disclosed in note 40 to the consolidated and separate financial statements, the corresponding figures for 30 June 2019 have been restated as a result of errors identified in the consolidated and separate financial statements of the municipality at, and for the year ended, 30 June 2020.

### **Material losses and impairment**

13. As disclosed in note 15 to the consolidated and separate financial statements, material impairment allowances of R2,6 billion (2019: R2,2 billion) and R1 billion (2019: R859,2 million) were made against trade receivables – exchange and non-exchange transactions respectively. The net movement in these impairment allowances together with the bad debts write-offs resulted in an impairment expense of R1,2 billion (2019: R759,1 million).

14. As disclosed in note 35.9 to the consolidated and separate financial statements, material water losses of R237,1 million (2019: R161.5 million) were incurred, which represented 46.3% (2019: 41.1%) of the total water cost. The non-technical losses of 8.8% were as a result of unauthorised consumption due to theft or illegal use.

15. As disclosed in note 35.10 to the consolidated and separate financial statements, material electricity losses of R558,6 million (2019: R484,2 million) were incurred, which represented 20.30% (2019: 15.47%) of the total electricity purchased. The non-technical losses of 14.3% were as a result of faulty meters, theft through illegal connections and meter tampering.

### **Underspending on conditional grants**

16. As disclosed in note 22.16 to the consolidated and separate financial statements, the urban settlement development grant had an unspent portion amounting to R307,3 million. The grant is used to improve urban land production to the benefit of poor households as well as improving spatial integration and densities.

17. As disclosed in note 22.21 to the consolidated and separate financial statements, the drought relief grant has an unspent portion amounting to R188,1 million. The grant is used for responding to the community's needs with the aim to alleviate the consequences of drought within the municipality.

### **Other matter**

18. I draw attention to the matter below. My opinion is not modified in respect of this matter.

## Unaudited disclosure note

19. In terms of section 125(2)(e) of the MFMA, the municipality and its municipal entity are required to disclose particulars of non-compliance with the MFMA in the consolidated and separate financial statements. This disclosure requirement did not form part of the audit of the consolidated and separate financial statements and, accordingly, I do not express an opinion on it.

## Responsibilities of the accounting officer for the consolidated and separate financial statements

20. The accounting officer is responsible for the preparation and fair presentation of the consolidated and separate financial statements in accordance with the SA Standards of GRAP and the requirements of the MFMA and Dora and for such internal control as the accounting officer determines is necessary to enable the preparation of consolidated and separate financial statements that are free from material misstatement, whether due to fraud or error.

21. In preparing the consolidated and separate financial statements, the accounting officer is responsible for assessing the group's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the appropriate governance structure either intends to liquidate the group or to cease operations, or has no realistic alternative but to do so.

## Auditor-general's responsibilities for the audit of the consolidated and separate financial statements

22. My objectives are to obtain reasonable assurance about whether the consolidated and separate financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated and separate financial statements.

23. A further description of my responsibilities for the audit of the consolidated and separate financial statements is included in the annexure to this auditor's report.

## Report on the audit of the annual performance report

### Introduction and scope

24. In accordance with the Public Audit Act 25 of 2004 (PAA) and the general notice issued in terms thereof, I have a responsibility to report on the usefulness and reliability of the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report. I performed procedures to identify material findings but not to gather evidence to express assurance.

25. My procedures address the usefulness and reliability of the reported performance information, which must be based on the municipality's approved performance planning documents. I have not evaluated the completeness and appropriateness of the performance indicators/measures included in the planning documents. My procedures do not examine whether the actions taken by the municipality enabled service delivery. My procedures also do not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.

26. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected development priority presented in the municipality's annual performance report for the year ended 30 June 2020:

Development priority	Pages in the annual performance report
KPA 1- basic service delivery	x – x

27. I performed procedures to determine whether the reported performance information was properly presented and whether performance was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.

28. The material findings in respect of the usefulness and reliability of the selected development priority are as follows:

#### Various indicators

29. The targets for the indicators listed below per the approved service delivery and budget implementation plan were changed without the necessary approval and were therefore not consistent with the initially approved targets.

Indicator number	Indicator description	Initial target	Revised target
KPI 3	Number of boreholes drilled	100%	5
KPI 4	Percentage completion of Loerie Water Treatment Works Upgrade	30%	70%
KPI 5	Percentage completion of Seaview Pump Station Upgrade	60%	95%
KPI 10	Percentage of industries with trade effluent inspected for compliance	100% by December 2019	100%
KPI 50	Km of sewer pipelines augmented	3km	0.6km

### Various indicators

30. The indicators and targets listed below did not agree to the planned indicators and targets as per the approved budget implementation plan, as these indicators were not reported on in the annual performance report.

Indicator number	Indicator description	Target
KPI 6	Km of water pipelines augmented	5km
KPI 7	Percentage completion of Coegakop Water Treatment Works construction	25%
KPI 12	Percentage completion of the Cape Recife Waste Water Treatment Upgrade	40% (Cape Recife: Phase 2)

### Various indicators

31. I was unable to obtain sufficient appropriate audit evidence that systems and processes had been established to enable consistent measurement and reliable reporting of performance against predetermined indicator definitions. This was due to insufficient measurement definitions and processes. As a result, I was also unable to obtain sufficient appropriate audit evidence for the achievements reported in the annual performance report. I was unable to confirm these achievements by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievements for the indicators listed below.

Indicator number	Indicator description	Planned target	Reported achievement
KPI 8	Percentage of complaints/callouts responded to within 24 hours (sanitation/wastewater)	100%	98.19%
KPI 9	Percentage of complaints/ callouts responded to within 24 hours (water)	100%	94.44%

### KPI 50 – Km of sewer pipelines augmented

32. I was unable to obtain sufficient appropriate audit evidence for the achievement of 0.6km reported against the target of 0.6km in the annual performance report due to the lack of accurate and complete records. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievement.

### Various indicators

33. The achievements reported in the annual performance report materially differed from the supporting evidence provided for the indicators listed below.

Indicator description	Reported achievement	Audited value
KPI 2 – Number of water connections meeting minimum standards	1468 in line with housing programme	979
KPI 49 – Number of new sewerage connections meeting minimum standard	1468 in line with housing programme	979

## Other matters

34. I draw attention to the matters below.

### Achievement of planned targets

35. Refer to the annual performance report on pages ... to ... for information on the achievement of planned targets for the year. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs 29 to 33 of this report.

### Adjustment of material misstatements

36. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were in the reported performance information of KPA 1 – basic service delivery. As management subsequently corrected only some of the misstatements, I raised material findings on the usefulness and reliability of the reported performance information. Those that were not corrected are reported above.

## Report on the audit of compliance with legislation

### Introduction and scope

37. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the municipality's compliance with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.

38. The material findings on compliance with specific matters in key legislation are as follows:

### Annual financial statements

39. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. A material misstatement of a disclosure item identified by the auditors in the submitted financial statements of the municipality was subsequently corrected or the supporting records provided, but the uncorrected material misstatements and supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.

### Strategic planning and performance management

40. The performance management system and related controls were inadequate as it did not describe how the performance monitoring, measurement, review, reporting and improvement processes should be conducted, as required by municipal planning and performance management regulation 7(1).

41. The service delivery and budget implementation plan was revised during the year without approval of the council following approval of an adjustments budget, as required by section 54(1)(c) of the MFMA.



## Asset management

42. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.

## Revenue management

43. Interest was not charged on all accounts in arrears, as required by section 64(2)(g) of the MFMA.

## Expenditure management

44. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
45. Reasonable steps were not taken to prevent irregular expenditure amounting to R1,3 billion as disclosed in note 44.2 to the financial statements of the municipality, as required by section 62(1)(d) of the MFMA. The majority of the irregular expenditure was caused by non-compliance with Supply Chain Management (SCM) Regulations.
46. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R30,1 million, as disclosed in note 44.1 to the financial statements of the municipality, in contravention of section 62(1)(d) of the MFMA. The majority of the unauthorised expenditure was caused by the overspending of the total amount appropriated for a vote in the approved budget.

## Consequence management

47. Irregular expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.
48. Fruitless and wasteful expenditure incurred by the municipality was not all investigated to determine if any person is liable for the expenditure, as required by section 32(2)(b) of the MFMA.
49. Losses resulting from fruitless and wasteful expenditure were not recovered from the liable person, as required by section 32(2)(b) of the MFMA.

## Procurement and contract management

50. Some goods and services with a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a). Deviations were approved by the accounting officer even though it was not impractical to invite competitive bids, in contravention of SCM regulation 36(1). Similar non-compliance was also reported in the prior year.
51. Bid specifications for some tenders were drafted in a biased manner and did not allow all potential suppliers to offer their goods or services, in contravention of SCM regulation 27(2)(a).

52. The performance of some contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA. Similar non-compliance was also reported in the prior year.

### Other information

53. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report. The other information does not include the consolidated and separate financial statements, the auditor's report and those selected development priorities presented in the annual performance report that have been specifically reported in this auditor's report.

54. My opinion on the consolidated and separate financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion on it.

55. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated and separate financial statements and the selected development priorities presented in the annual performance report or my knowledge obtained in the audit, or otherwise appears to be materially misstated.

56. If based on the work I have performed, I conclude that there is a material misstatement in this other information, I am required to report that fact. I have nothing to report in this regard.

### Internal control deficiencies

57. I considered internal control relevant to my audit of the consolidated and separate financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance on it. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the qualified opinion, the findings on the performance report and the findings on compliance with legislation included in this report.

58. There was instability at the leadership and management level of the municipality. In addition, leadership did not stabilise the internal control environment through their oversight role to enable effective reporting on the municipality's financial and performance results, and to ensure compliance with legislative requirements.

59. Management did not consistently implement daily, weekly and monthly financial and performance management disciplines. In addition, key risks relating to financial and performance reporting as well as supply chain management were not actively managed during the year under review.

60. Management's review and monitoring processes over compliance were not effective to ensure compliance with legislative requirements.

## Material irregularities

61. In accordance with the PAA and the Material Irregularity Regulations, I have a responsibility to report on material irregularities identified during the audit.

### Material irregularities identified during the audit

62. The material irregularities identified are as follows:

#### Interest not charged on debtors

63. The municipality did not charge interest on arrears. Debtors who had entered into long-term arrangement agreements with the municipality were not charged interest in the 2018-19 financial year. This resulted in a non-compliance with section 64(2)(g) of the MFMA which requires that the municipality charge interest on arrears, except where the council had granted exemptions. The municipality is likely to suffer a material financial loss if interest is not charged on the outstanding accounts and the debt is not recovered.

64. The accounting officer was notified of the material irregularity on 9 December 2019 and invited to make a written submission on the actions taken or to be taken to address the matter.

65. The following actions have been taken to resolve the material irregularity:

- A preliminary investigation completed in February 2020 by the billing coordination division in consultation with the debtor management division determined that the accounting system was not charging interest on the capital portion that is subjected to the arrangement. The outcome of the investigation also indicated that the material irregularity is a result of a system deficiency.
- Programming was undertaken in February 2020 to the accounting system to raise interest every month when an instalment is raised. The raising of interest on arrangement debt is now an inherent part of the of the municipalities accounting system. The municipality is currently raising interest on all its interest bearing long term arrangements with effect from February 2020.

66. The accounting officer plans to prepare and table a detailed item to budget and treasury standing committee in June 2021 and to council for consideration and approval that interest on arrangements not be raised retrospectively for the period where the accounting system was unable to raise interest on arrangements.

67. The implementation of the above planned action will be further followed up during the next audit.

### Payment for services not received: Storm-water drain cleaning

68. The municipality paid R10,1 million on 19 December 2018 for the provision of storm-water drain cleaning services which were not rendered to the municipality. This resulted in a non-compliance with section 65(2)(a) of the MFMA which requires that the municipality have and maintain an effective system of expenditure control relating to the approval, authorisation, and payment of funds. The non-compliance with legislation is likely to result in a material financial loss if the municipality does not recover the money paid to the service provider.
69. The accounting officer was notified of the material irregularity on 13 December 2019 and invited to make a written submission on the actions taken or to be taken to address the matter.
70. An investigation into the matter by the provincial Hawks unit commenced in January 2020 and the municipality is co-operating with the investigation. On conclusion of the investigation, the municipality is planning to take possible recovery of losses incurred and consequence management against the identified responsible official(s). I will follow up on the investigation and the implementation of the planned actions during my next audit.

### Payment for services not received: Storm-water drain cleaning

71. The municipality paid R10,1 million on 19 December 2018 for the provision of storm-water drain cleaning services which were not rendered to the municipality. This resulted in a non-compliance with section 65(2)(a) of the MFMA which requires that the municipality have and maintain an effective system of expenditure control relating to the approval, authorisation, and payment of funds. The non-compliance with legislation is likely to result in a material financial loss if the municipality does not recover the money paid to the service provider
72. The accounting officer was notified of the material irregularity on 13 December 2019 and invited to make a written submission on the actions taken or to be taken to address the matter.
73. An investigation into the matter by the provincial Hawks Unit commenced in January 2020 and the municipality is co-operating with the investigation. On conclusion of the investigation, the municipality is planning to take appropriate consequence management steps against the identified responsible official(s). I will follow up on the investigation and the implementation of the planned actions during my next audit.

### **Material irregularities in progress**

74. I identified a material irregularity during the audit and notified the accounting officer thereof as required by material irregularity regulation 3(2). By the date of this auditor's report, I had not yet completed the process of evaluating the responses from the accounting officer. This material irregularity will be included in the next year's auditor's report.

## Other reports

75. In addition to the investigations relating to material irregularities, I draw attention to the following engagements conducted by various parties which had, or could have, an impact on the matters reported in the municipality's consolidated and separate financial statements, reported performance information, compliance with applicable legislation and other related matters. These reports did not form part of my opinion on the consolidated and separate financial statements or my findings on the reported performance information or compliance with legislation.
76. In the current year, the Special Investigations Unit conducted an investigation into the construction of toilets meant for informal settlements, in response to the covid-19 pandemic. Not all SCM processes had been followed in the appointment of the service provider. Legal proceedings are in progress to prevent the municipality from proceeding with the contract.

*Auditor - General*

East London

16 April 2021



AUDITOR - GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*

## **Annexure – Auditor-general’s responsibility for the audit**

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the consolidated and separate financial statements and the procedures performed on reported performance information for selected development priorities and on the municipality’s compliance with respect to the selected subject matters.

### **Financial statements**

2. In addition to my responsibility for the audit of the consolidated and separate financial statements as described in this auditor’s report, I also:
  - identify and assess the risks of material misstatement of the consolidated and separate financial statements, whether due to fraud or error; design and perform audit procedures responsive to those risks; and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations or the override of internal control
  - obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the group’s internal control
  - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer
  - conclude on the appropriateness of the accounting officer’s use of the going concern basis of accounting in the preparation of the consolidated and separate financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists relating to events or conditions that may cast significant doubt on the ability of the municipality and its subsidiaries to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor’s report to the related disclosures in the consolidated and separate financial statements about the material uncertainty or, if such disclosures are inadequate, to modify my opinion on the financial statements. My conclusions are based on the information available to me at the date of this auditor’s report. However, future events or conditions may cause a group to cease operating as a going concern
  - evaluate the overall presentation, structure and content of the consolidated and separate financial statements, including the disclosures, and determine whether the consolidated and separate financial statements represent the underlying transactions and events in a manner that achieves fair presentation
  - obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the group to express an opinion on the consolidated and separate financial statements. I am responsible for the direction, supervision and performance of the group audit. I remain solely responsible for my audit opinion.

## **Communication with those charged with governance**

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.
4. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and, where applicable, the actions taken to eliminate threats or the safeguards applied.